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COMPUTEL SYSTEMS LTD. 1969 ANNUAL REPORT

To the Shareholders

Your company's second fiscal year which ended on August 31, 1969 has been a year of rapid growth both in computing capacity and in technical strength. On the other hand the financial results have been disappointing.

At the beginning of the year, Computel had one Univac 1108 computer in operation located in Ottawa and a total staff of 26. In February two new Utility Centres were opened with the installation of a Univac 1108 computer in Toronto and an IBM 360, model 65 computer in Ottawa; a hardware development laboratory was established and the company's software development group enlarged. As a result Computel now has a staff of over 120.

As anticipated, the company's expansion programme resulted in significantly higher operating and systems development costs. Unfortunately, revenues have not grown proportionally, with the result that substantial operating losses were incurred in the latter half of the year. Management

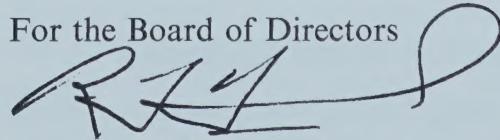
is making every effort to improve revenues and at the same time, is exploring other ways of improving the company's performance through cost reductions wherever possible.

The short term market outlook has been affected by the current review of expenditures by the Federal Government and by the announced entry into the industry of a number of newly created computer service companies. While competition from these companies has not yet had any significant effect upon revenues, there is the prospect of excess capacity in the industry during the next few years.

In the computer industry, more perhaps than in most others, ultimate success depends upon people. While Computel has experienced an exciting but difficult year, its staff of computer professionals has proven itself by hard work and enthusiasm for which your Board of Directors is most appreciative.

November 1, 1969

For the Board of Directors



Robert T. Horwood

Executive Vice-President and Secretary

Directors

Bernard D. Beamish
Warren D. Beamish
Frederick B. Brooks-Hill
George R. Cogar
Christopher G. Fleming
Robert T. Horwood
Charles E. O'Connor
Norman J. Short
Robert N. Steiner

Officers

Vice-President & Chief Executive Officer	Ronald T. Lane
Executive Vice-President & Secretary	Robert T. Horwood
Vice-President, Systems	Andrew M. Wyszkowski
Treasurer	Bernard D. Beamish
President, Computel Leasing Ltd.	Ronald T. Lane

AUDITORS

Clarkson, Gordon & Co.

REGISTRAR & TRANSFER AGENT

Canada Permanent Trust Company

LISTING

Toronto Stock Exchange

Offices & Principal Equipment

222 Laurier Avenue West, Ottawa 4. 746-4353	UNIVAC 1108
1200 St. Laurent Blvd., Ottawa 7. 746-4353	IBM 360 Model 65
250 Bloor Street East, Toronto. 929-9011	UNIVAC 1108
2100 Drummond Street, Montreal. 845-4706	Terminal/Marketing

Financial Review

COMPUTER TIME AND RELATED REVENUE

Computer utility revenue for the year amounted to \$2,168,950. While this amount is substantially higher than in the previous fiscal year, the two periods are not directly comparable because of the addition of two new Utility Centres to the network in February, 1969 and because the previous fiscal period was of seven months' duration only.

In late May of this year, the company completed a major non-recurring computing project which had during the preceding four months produced revenues in excess of \$100,000. The completion of this project, and the effect on revenue of the technical difficulties experienced with the Univac 1108 computer in Ottawa this past summer have resulted in a decline in operating revenues during the final quarter of the year.

As indicated, the company experienced technical difficulties at the Ottawa 1108 site which resulted in a complete suspension of operations for eight days in July. Further difficulties were experienced in September. These difficulties have since been overcome and the system is now performing satisfactorily. Because of Computel's back-up capability, the company was able to maintain service for all its customers.

LEASING CONTRACT REVENUE

Contract revenue earned from third parties by the company's wholly owned subsidiary, Computel Leasing Ltd., amounted

to \$60,705 this year, the subsidiary's first year of operations. During the year, Computel Leasing Ltd. purchased the two major computer systems added to the utility network by the parent company, and a number of smaller computers some of which are leased to outside users and others to the parent for use as remote terminals by customers of the network.

Computel Leasing has been following closely the effect of increased competition in the independent computer leasing industry and its effect upon rates of return available on lease contracts. As a result, the company has not actively sought new lease contracts for a number of months past, nor would conditions appear to warrant a change in this policy in the near future.

OPERATING COSTS

As expected, operating costs increased substantially during the year to reflect the expansion from one to three Utility Centres. While higher cost levels may be expected to continue in the future, certain other charges of a non-recurring nature were provided for during the current year.

The company has charged against income as incurred all of the costs associated with the two new Utility Centres opened during the year. This includes the substantial payroll and training costs required to recruit and train the necessary operating staff and the costs of leased space incurred prior to the dates the new centres became operational. These pre-operating costs amounted to approximately \$134,000 this

year. In addition, non-recurring charges for technical services and for extra maintenance amounting to approximately \$40,000 were incurred in the company's fourth quarter.

SYSTEMS DEVELOPMENT

It is the company's practice to charge software development costs against income as incurred. While long term benefits may frequently accrue as a result of these projects, it has been the company's experience that the requirement for systems software development is of a continuing nature if Computel is to keep abreast with customers' requirements.

During the year a number of projects were undertaken by the systems group to improve the operating performance of the utility network. Two of the more significant were the DART project and the port expansion project.

DART Project:

In January the company established a hardware development laboratory to design and build an improved communications adapter for the Univac 1004 remote terminal. It was expected that this device, if successful, would be used with almost all Computel terminals. In addition, an out-

side market was anticipated which would be sufficient to offset the costs of development. The first prototype DART device was planned for early April but was not completed until June, 1969. Since then, three production units have been built and are being used by selected remote terminal customers for testing purposes.

Port Expansion Project:

Initially, the number of terminal customers who could simultaneously access each 1108 system was limited to six. This limited the number of potential terminal customers and did not permit efficient utilization of the central processor under most operating conditions.

The Systems Software group has developed a method permitting an increase from six to twelve input ports utilizing small general purpose computers which transmit data from remote terminals to the central system and back. The expansion project was initially expected to be in full operation by July on the Ottawa system and by August in Toronto. However deliveries of equipment were later than expected and when the equipment did arrive, the arrival dates coincided with the technical difficulties described earlier which caused a further delay in implementing the project. It is hoped that the Ottawa system expansion will be operational by the end of 1969.

Auditors' Report

To the Shareholders of
Computel Systems Ltd.:

We have examined the consolidated balance sheet of Computel Systems Ltd. as at August 31, 1969 and the consolidated statements of income and deficit and source and application of funds for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion these consolidated financial statements present fairly the financial position of the companies as at August 31, 1969 and the results of their operations and the source and application of their funds for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Ottawa, Canada,
October 2, 1969.

Clarkson, Gordon & Co.

CLARKSON, GORDON & CO.
Chartered Accountants



Consolidated Balance Sheet

August 31, 1969

ASSETS

Current:

	1969	1968
	\$	\$
Cash	24,600	45,032
Short term investments (at cost which approximates market)	1,100,000	—
Accounts receivable	615,248	44,504
Prepaid expenses	25,020	15,389
	<hr/> <u>1,764,868</u>	<hr/> <u>104,925</u>

Fixed, at cost: (note 3)

Computer and ancillary equipment	8,668,772	2,227,675
Furniture and fixtures	144,248	15,543
Leasehold improvements	216,175	39,738
	<hr/> <u>9,029,195</u>	<hr/> <u>2,282,956</u>
Less accumulated depreciation	689,972	145,106
	<hr/> <u>8,339,223</u>	<hr/> <u>2,137,850</u>

Other, at cost:

Pre-operating expenses	—	38,427
Bond, debenture and share issue expenses (less amortization)	339,496	74,099
Incorporation expense	5,772	5,772
	<hr/> <u>345,268</u>	<hr/> <u>118,298</u>
	<hr/> <u>\$10,449,359</u>	<hr/> <u>\$2,361,073</u>

On behalf of the Board:

B. D. BEAMISH, *Director*

R. T. HORWOOD, *Director*

COMPUTEL SYSTEMS LTD.
 and its wholly-owned subsidiary Computel Leasing Ltd.
 (Incorporated under the laws of Canada)

statement 1

LIABILITIES

Current:

Bank loan (against which accounts receivable have been pledged as collateral)
 Accounts payable and accrued charges
 Accrued bond and debenture interest
 Taxes payable.
 Current portion of long-term debt

1969	1968
\$	\$
—	25,000
612,678	69,701
148,773	15,187
29,584	3,646
—	193,000
<u>791,035</u>	<u>306,534</u>

Long-term debt (note 1):

9% first mortgage sinking fund bonds,
 due January 15, 1975
 6% convertible subordinated debentures
 due September 15, 1988
 Less sinking fund instalment
 due within one year

964,000	1,350,000
5,000,000	—
—	193,000
<u>5,964,000</u>	<u>1,157,000</u>

SHAREHOLDERS' EQUITY:

Capital stock (note 2)—

Authorized:

1,000,000 common shares without nominal
 or par value

Issued:

581,142 shares
 Deficit (statement 2)

4,229,997	990,791
(535,673)	(93,252)
<u>3,694,324</u>	<u>897,539</u>
<u>\$10,449,359</u>	<u>\$2,361,073</u>

(See accompanying notes to financial statements)



statement 2

Consolidated Statement of Income and Deficit

For the year ended August 31, 1969

(with comparative figures for the seven month period ended August 31, 1968)

INCOME:

	1969	1968
	\$	\$
Computer time and related charges	2,168,950	486,474
Leasing contract revenue	60,705	—
Income from short-term investments	280,265	—
	<u>2,509,920</u>	<u>486,474</u>

EXPENSES, including depreciation (note 3):

Operations costs	2,073,420	419,713
Administrative and systems expenses	446,986	66,386
Amortization of pre-operating expenses	38,427	21,145
Bond and debenture interest, net of interest capitalized	393,508	72,482
	<u>2,952,341</u>	<u>579,726</u>

Net loss for the year	442,421	93,252
Deficit, beginning of year	<u>93,252</u>	—
Deficit, end of year	<u>\$ 535,673</u>	<u>\$ 93,252</u>

(See accompanying notes to financial statements)

COMPUTEL SYSTEMS LTD.
and its wholly-owned subsidiary Computel Leasing Ltd.

statement 3

Consolidated Statement of Source and Application of Funds

For the year ended August 31, 1969

(with comparative figures for the seven month period ended August 31, 1968)

SOURCE OF FUNDS:

From operations—

	1969	1968
	\$	\$
Loss for the period	(442,421)	(93,252)
Depreciation	544,866	145,106
Amortization of bond, debenture and share issue expenses	24,647	7,464
Amortization of pre-operating expenses	38,427	21,145
	<hr style="border-top: 1px solid black; border-bottom: none; border-left: none; border-right: none; margin-bottom: 5px; margin-top: 5px;"/>	<hr style="border-top: 1px solid black; border-bottom: none; border-left: none; border-right: none; margin-bottom: 5px; margin-top: 5px;"/>
Bonds issued	165,519	80,463
Shares issued	—	1,350,000
Debentures issued	3,239,206	990,791
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	5,000,000	—
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	8,404,725	2,421,254

APPLICATION OF FUNDS:

Purchase of fixed assets	6,746,239	2,282,956
Pre-operating expenses	—	59,572
Bond Debenture and share issue expenses	290,044	81,563
Incorporation expense	—	5,772
Redemption of bonds	193,000	193,000
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Increase (decrease) in working capital during the year	7,229,283	2,622,863

\$1,175,442

\$ (201,609)

(See accompanying notes to financial statements)



Notes to Consolidated Financial Statements August 31, 1969

1. LONG-TERM DEBT: Under the terms of the Trust Deed securing the 9% first mortgage sinking fund bonds, annual sinking fund instalments of \$193,000 are required to January 15, 1975. The instalment due January 15, 1970 was provided for during the year through the purchase of bonds on the open market. In addition the Company may, at its option, redeem bonds at any time prior to maturity at prices ranging from 108% of the principal amount if redeemed on or before January 15, 1970, to 100% of the principal amount if redeemed after January 15, 1974.

Debentures—

Under the terms of the Trust Indenture securing the 6% convertible subordinated debentures, the Company is required to retire through the operation of a sinking fund \$500,000 principal amount of debentures in each of the years 1979 to 1987 inclusive. These debentures are convertible into common shares at a conversion rate of 28 shares for each \$1,000 principal amount of debentures at any time prior to September 15, 1978. In addition, the Trust Indenture provides that the Company may at its option redeem debentures at any time prior to maturity at prices ranging from 106% of the principal amount if redeemed on or before September 14, 1969, to 100% of the principal amount if redeemed after September 14, 1987.

The Company may not pay any cash dividends on its common shares until all of the first mortgage bonds and the convertible subordinated debentures have been retired.

2. CAPITAL STOCK:

During the year, 81,142 common shares of the capital stock of the Company were issued for cash of \$3,239,206.

Options have been granted to certain employees of the Company and its subsidiary to purchase in the aggregate 25,675 shares at prices ranging from \$16 to \$41 per share at various expiry dates prior to July 16, 1974. A total of 165,675 shares have been reserved for the above stock options and for the conversion of the 6% convertible subordinated debentures.

On November 22, 1968, the Company was granted Supplementary Letters Patent increasing the amount for which it may issue its shares from \$7,000,000 to \$10,000,000.

COMPUTEL SYSTEMS LTD.
and its wholly-owned subsidiary Computel Leasing Ltd.

3. DEPRECIATION:

Depreciation of computers and the major portion of the ancillary equipment has been provided, from the dates of acceptance from the manufacturers, on the basis of an eight year life with provision for a 15% residual or salvage value. Two of the Company's three major computers were accepted from the manufacturers in the latter part of the year. Depreciation charged against income in the year ended August 31, 1969 amounted to \$544,866.

4. COMMITMENTS:

Equipment—

As at August 31, 1969 the Company has commitments to acquire further computer and ancillary equipment for amounts which aggregate approximately \$1,225,000.

Other—

The Company occupies leased premises under agreements of from one to four years' duration. The total annual rent payable under these agreements is \$128,600. In addition, the Company leases equipment and has contracted for prime shift maintenance services for its computers. The current rates for these annual lease and maintenance charges on equipment aggregate approximately \$220,000 and \$283,000 respectively.

**5. STATUTORY
INFORMATION:**

Remuneration paid to directors of the Company as officers and employees amounted to \$34,000. No remuneration was paid to directors as such.

FINANCIAL STATEMENTS
(Unaudited)

CONSOLIDATED INCOME

	Three Months Ended	Six Months Ended	
	Nov. 30/68	Feb. 28/69	Feb. 28/69
Operating revenue	\$331,674	\$477,467	\$809,141
Operating expenses	266,644	443,666	710,310
Operating income	65,030	33,801	98,831
Interest and other income	70,697	112,320	183,017
	135,727	146,121	281,848
Bond and debenture interest ..	92,875	105,375	198,250
Pre-operating expenses for new utility centres	39,216	94,836	134,052
Net profit (loss) for the period, before tax	\$ 3,636	\$(54,090)	\$(50,454)

CONSOLIDATED SOURCE AND APPLICATION OF FUNDS

Source of Funds			
Net profit (loss)	\$ 3,636	\$(54,090)	\$(50,454)
Add non-cash charges			
Depreciation	72,039	96,048	168,087
Other	16,426	17,264	33,690
From operations	92,101	59,222	151,323
Debentures issued	5,000,000		5,000,000
Shares issued	3,219,576	19,630	3,239,206
Minority interest in subsidiary		2,000	2,000
	8,311,677	80,852	8,392,529

Application of Funds

Purchase of fixed assets	300,582	2,996,750	3,297,342
Current portion of long term debt		193,000	193,000
Increase in other assets (Net)	298,573	17,793	316,366
	599,155	3,207,553	3,806,708
Increase in Working Capital ..	\$ 7,712,522	\$(3,126,701)	\$ 4,585,821

OFFICERS AND DIRECTORS

OFFICERS

President Warren D. Beamish
Executive Vice-President Robert T. Horwood
Vice-President Systems Software... Andrew M. Wyskowski
President Computel Leasing Ronald T. Lane

DIRECTORS

Bernard D. Beamish
Warren D. Beamish
Frederick B. Brooks-Hill
George R. Cogar
Christopher G. Fleming
Robert T. Horwood
Charles E. O'Connor
Norman J. Short
Robert N. Steiner

OFFICES

OFFICES	PRINCIPAL EQUIPMENT
222 Laurier Avenue West, Ottawa 4. 237-0565	UNIVAC 1108
1700 St. Laurent Blvd., Vanier City. 237-0565	IBM 360/65
250 Bloor Street East, Toronto 5. 929-9011	UNIVAC 1108
2100 Drummond Street, Montreal 25. 845-4706	Terminal/Marketing

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REPORT

TO THE SHAREHOLDERS

2nd QUARTER

FOR THE PERIOD ENDING

FEBRUARY 28, 1969

Computel Systems Ltd.,
222 Laurier Ave. West,
Ottawa 4, Ont.

REPORT TO THE SHAREHOLDERS

Your company has completed the second quarter of its first full year. During this quarter Computel has trebled both staff and equipment to three major utility centres to become the largest integrated user of computing equipment in Canada.

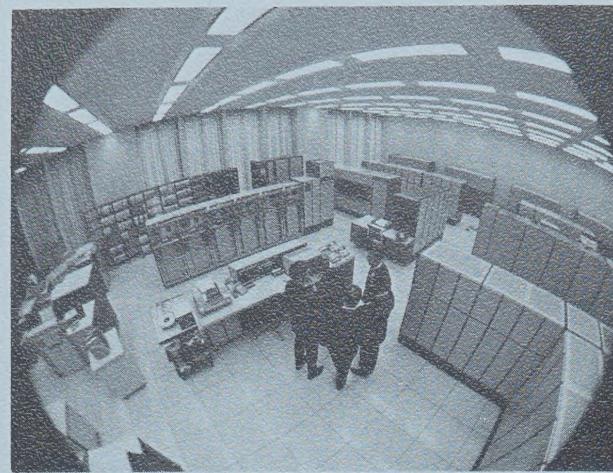
In September 1968, after the Company had reached a profitable monthly level, decisions were taken to install a UNIVAC 1108 Computer in Toronto and an IBM 360/65 System in Ottawa. The pre-operating expenses of \$134,052 prior to commencement of business February 1969 were absorbed on a current basis resulting in a net loss for each of the months November '68 through January '69.

The quarter includes the first operating month of the two new installations. The company does not anticipate installation of additional major equipment during the current fiscal year. It is not possible to predict performance based on one month, however, the results on all equipment are most encouraging.

CORPORATE STRUCTURE

Coincidental with the plans to expand from one to three utility centres, a major corporate re-organization took place. Mr. R. T. Horwood was made Executive Vice-President and four Vice-Presidential responsibility areas were defined, covering Finance and Administration, Marketing, Systems Software and Systems Hardware. Mr. A. M. Wyszkowski was promoted to Vice-President Systems Software and Mr. F. S. Mallett C.A. is joining the company assuming the duties of Vice-President, Finance and Administration.

Joining the company and bringing considerable IBM 360/65 experience, were Mr. R. R. Rothgeb as Director and Mr. O. J. Woodland, Manager, Customer Support. Mr. J. C. Glover assumed responsibilities as Manager, Toronto Branch.



The Toronto UNIVAC 1108 Utility Centre opened February 1, 1969 under the direction of John Glover, Manager.

THE COMPUTER UTILITY

Computel's business is the creation of a product; computing power. In the field of Computer Services most companies essentially provide a service, solving a problem at a fixed price. Included are management consultants, application programmers and computer service bureaus.

Independent programmers using Computel have strengthened their business. During this quarter the first independent service organization, Kurtz and Steel Ltd., contracted for a 1004 terminal to the network. Kurtz and Steel Ltd., located in Sheridan Park, provide Critical Path Consulting, programming and other services. Other computer service organizations are negotiating for Computel terminals.

Consistent with the creation and distribution of Computing Power, Computel is concerned with: Efficient Cost/Performance Terminal Equipment, Data Communications, Modulating Equipment and Communication Interfaces.

Computel competes with computer manufacturers for the provision of facilities which allow a customer to tackle computer oriented problems. The manufacture, assembly or creation of components in any of the above areas is entirely consistent with corporate objectives.

DEVELOPMENT AND FORWARD PLANNING

Since February 1968 Computel personnel has been engaged in optimizing the performance of the 1108 and its inter-relation with the 1004 terminals. Coincidental with the decision to build a multi-system network certain functional and operational problems were identified. Load levelling, system overhead reduction and system inter-compatibility present challenges which will only be addressed by development dollars from a utility company.

During the second quarter Computel has created a Design/Development laboratory under the direction of Dr. Warren Smith, a PhD in Electrical Engineering.

Within the Systems Hardware Division, the company allows for the logical development into full maintenance operations and productions or manufacturing. In the latter area the company has contracted to have sub-assemblies built and installed to modify purchased equipment.

In the Systems Software Division, research and development is being carried out with the goal of extending the applicability of operating systems and compilers to new environments. This work is intended to ensure a strong position for Computel in a changing marketplace.



Tony Zimmer, Warren Smith and Gene Kaczor in Computel's Laboratory in Ottawa.